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Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-03
INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02 OPIC-03
SP-02 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04
CEA-01 /080 W
----------272313Z 014500 /22
R 271638Z APR 77
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC 3260
INFO AMEMBASSY BERN
AMEMBASSY BONN
AMEMBASSY LONDON
AMCONSUL MONTREAL
ALL OTHER CONSULATES IN CANADA (BY POUCH)

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DEPT PASS TREASURY, FRB

E.O. 11652: N/A
TAGS: EFIN, CA
SUBJECT: FURTHER VIEWS ON FINANCING QUEBEC BUDGET DEFICIT

REF: A. OTTAWA 2864; B. QUEBEC 154; C. MONTREAL 334

1. SUMMARY: CONSENSUS GROWING THAT QUEBEC'S DIRECT BORROWING REQUIREMENT FORECAST IN PROVINCIAL BUDGET OF DOLS 900 MILLION WAS UNDERSTATED BY DOLS 300 TO DOLS 400 MILLION. HOWEVER, AT LEAST ONE PROMINANT BANK BELIEVES PROVINCE WILL BE ABLE TO MEET HIGHER REQUIREMENT WITHOUT UNDUE PROBLEMS, HELPED IN PART BY DOLS 300 MILLION EURO-DOLLAR LOAN FOR QUEBEC ANNOUNCED APRIL 23. END SUMMARY.

2. ROYAL BANK ESTIMATES THAT RECEIPTS FORECAST IN QUEBEC BUDGET WERE OVERESTIMATED BY ABOUT DOLS 200 MILLION,
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LARGELY BECAUSE ECONOMIC GROWTH IN PROVINCE WILL BE SLOWER THAN FORECAST. IN ADDITION, SPENDING MAY BE AS MUCH AS DOLS 200 MILLION HIGHER THAN ESTIMATED, IN PART BECAUSE OF HIGHER UNEMPLOYMENT AND WELFARE COSTS. IT THEREFORE CONCLUDES DIRECT PROVINCIAL BORROWING REQUIREMENT IN COMING FISCAL YEAR WILL BE DOLS 1.2 TO DOLS 1.3 BILLION RATHER THAN DOLS 900 MILLION FORECAST BY QUEBEC FINANCE

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MINISTER PARIZEAU. IT EXPECTS TWO SUPPLEMENTAL BUDGETS TO BE INTRODUCED IN THE COURSE OF THE YEAR TO COVER HIGHER SPENDING.

3. HOWEVER, BANK DOES NOT NOW EXPECT PROVINCE WILL ENCOUNTER DIFFICULTY IN BORROWING NECESSARY FUNDS. PROVINCE RECEIVED BOOST BY ANNOUNCEMENT OVER WEEKEND OF DOLS 300 MILLION BANK LOAN IN LONDON THROUGH MANAGEMENT GROUP LED BY ORION BANK LTD., A CONSORTIUM BANK IN WHICH THE ROYAL BANK OF CANADA HAS AN INTEREST. LOAN DESCRIBED BY BANKER AS "A VERY GOOD DEAL" FOR QUEBEC. TERMS ARE FOR SEVEN YEAR LOAN AT A FLOATING INTEREST RATE AT 1.125 PERCENT ABOVE LONDON INTERBANK OFFER RATE (LIBOR) FOR THE FIRST TWO YEARS AND 1.25 PERCENT ABOVE LIBOR FOR REMAINING FIVE YEARS. LOAN IS TO BE DRAWN DOWN IN INSTALLMENTS (POSSIBLY DOLS 100 MILLION EVERY OTHER WEEK FOR SIX WEEKS ACCORDING TO THE PRESS) WITH FIRST INSTALLMENT DATED MAY 15.

4. IN ADDITION TO THIS LOAN, ROYAL BANK ESTIMATES THAT ABOUT DOLS 300 MILLION CAN BE PLACED WITH THE CAISSE DE DEPOT WHICH ADMINISTERS QUEBEC PENSION PLAN. (CAISSE PURCHASED DOLS 395 MILLION OF QUEBEC BONDS IN CALENDAR 1976, WHILE TOTAL ASSETS GREW DOLS 1 BILLION IN SAME PERIOD). IN ADDITION, ROYAL BANK ESTIMATES DOLS 200 MILLION NET OF QUEBEC SAVINGS BONDS CAN BE SOLD. WITH ESTIMATES OF BORROWING REQUIREMENT RANGING FROM DOLS 900 MILLION TO DOLS 1.3 BILLION, THIS WOULD LEAVE DOLS 100 TO DOLS 500 MILLION TO BE FINANCED PRIMARILY THROUGH LIMITED OFFICIAL USE

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PUBLIC BOND SALES, AN AMOUNT ROYAL BANK BELIEVES MARKET COULD ABSORB WITHOUT UNDUE STRESS.

5. COMMENT. UNDERWRITERS BELIEVE EUROPEAN ACCEPTANCE OF QUEBEC PROVINCIAL DEBT PREDICATED ON BELIEF THAT HYDRO-QUEBEC AT LEAST WILL BE ABLE TO MAINTAIN ACCESS TO NEW YORK MARKET. SHOULD HYDRO-QUEBEC ENCOUNTER MAJOR DIFFICULTIES IN NEW YORK LATER THIS SPRING, PROVINCE COULD FIND FURTHER ACCESS TO EUROPE GREATLY REDUCED. ENDERS

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